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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1933.

No. 400

CITY OF MARION, ILLINOIS, A MUNICIPAL CORPORATION; CONTINENTAL ILLINOIS BANK & TRUST COMPANY, A CORPORATION; THE FIDELITY & CASUALTY COMPANY OF NEW YORK *et al.*,

Petitioners,

versus

BEN SNEEDEN, AS RECEIVER OF THE CITY NATIONAL BANK OF HERRIN, ILLINOIS,

Respondent.

CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

BRIEF OF LELAND K. NEEVES, AS AMICUS CURIAE.

THE GUNTHORP-WARREN PRINTING COMPANY, 310 WEST JACKSON, CHICAGO

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To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The writer of this brief filed a brief in the court below as *amicus curiae*. He represents the receiver of an Illinois state bank in proceedings pending in the United

States District Court for the Northern District of Illinois, Eastern Division, involving the question as to the right of a bank organized under the General Banking Act of Illinois to pledge assets to secure deposits made by the County Treasurer of Lake County, Illinois. There is no decision of the Supreme Court of Illinois dealing with the question so far as it relates to banks organized under the General Banking Act. The decision of the present case, involving as it may a determination of the Illinois law upon the subject, is therefore of large and far reaching importance.

This case with No. 128 involves the following questions:

(1) Whether a national bank under the provisions of the National Banking Act, apart from the 1930 amendment, has power to pledge its assets to secure deposits, either public or private;

(2) Does the 1930 amendment have the effect of making the local law determinative in the case of a national bank in the case of deposits of public moneys of the state or political subdivision thereof;

(3) Has a bank in Illinois organized under the General Banking Act power to pledge its assets to secure deposits of public moneys.

A procedural question is also involved as to the right of a receiver of a bank to recover the assets thus pledged without payment of the deposit.

STATEMENT OF THE CASE.

The facts of this case are fully set forth in the respective briefs of the petitioners and of the respondent. We stress the following: That the bonds in question, admittedly the property of the bank, were directly pledged as security for the deposits made or to be made by Carroll, as Treasurer of the City of Marion. The surety company here involved was the surety upon the City Treas-

urer's general bond. If the surety is required to pay to the City of Marion the amount of the deposit, it, as surety, would have recourse against the principal debtor, viz. the City Treasurer. In the present controversy, therefore, the pledge is sought to be enforced on behalf of Carroll who is responsible to the City as between it and the City and the claim of the surety company is, therefore, one of exoneration of its own liability as surety. The bonds were placed in the custody of a third party, the Continental Illinois Bank and Trust Company. Respondent as Receiver of the bank now closed is seeking the return of the bank's own property as against the claims of petitioners as alleged lien claimants.

STATUTES INVOLVED.

The relevant federal statutes and the relevant provisions of certain Illinois statutes and of the Illinois constitution are set out in the briefs of the respective parties and will not be repeated.

SUMMARY OF ARGUMENT.

Apart from special statutory authority for the pledging of assets by a national bank to secure deposits, either of public or private funds, the power, if it exists, must be found in the general provisions of the National Banking Act in Section 8 thereof. No distinction is there taken between public and private deposits; nor is the power in any way restricted or subject to limitation. The provisions of Section 45 of the National Banking Act in requiring the giving of security by national banks for deposits of public moneys of the United States and for the due performance of their duties as agents of the United States is of itself a delegation of power to national banks to give the security.

There is no general power in national banks to pledge their assets to secure private deposits. The recent tendency in authority is against the existence of such power.

A national bank has no general power to pledge its assets to secure public deposits. In the case of the United States there is no common law right of lien or even priority. Priority rests upon statute. Priority differs from specific lien in that priority is merely a right to be paid ahead of and to the total exclusion, if necessary, of ordinary creditors and depositors. A priority creditor, however, may be required to prorate with other priority creditors, if necessary. On the other hand, in the case of a lien creditor, the creditor is entitled to the exhaustion of the fund, if necessary, in order that his debt may be paid.

The 1930 amendment was intended to create, and has the legal effect of creating, parity between national and state banks within the same locality as to the giving of security for certain kinds of public deposits. It had the effect either of granting to national banks a power not theretofore existing, *i. e.* to pledge its assets to secure the deposits of a state or political subdivision thereof, provided a state bank within the same locality had such power, or, if the general power to make such a pledge theretofore existed, it limited and restricted such power to those cases where a state bank within the same locality could make such pledge. The form and phraseology of the amendment is indicative of such intention and such effect. Upon appellants' theory that the general power to pledge existed, then so far as any question is concerned as to the power of a national bank to make such a pledge the amendment is wholly surplusage. It could not possibly operate as an extension of the powers of national banks.

To consider the amendment, however, merely as restricting a power theretofore and otherwise existing, the conclusion would have to be that in the case of deposits of a different character, that is, deposits other than those of a state or political subdivision thereof, all of the power of a national bank theretofore and otherwise existing remains in full force. Therefore, national banks would retain the right to pledge their assets to secure private deposits but could not do so in the case of the deposits of the state or political subdivision thereof, unless a state bank within the same locality could make such pledge. No reason is suggested as to why the Congress should make such a distinction. All things considered a holding is seemingly required that the amendment intended to confer upon national banks a power to pledge assets to secure the deposits of a state or political subdivision thereof, provided a state bank within the same locality had such power and that such powers did not theretofore or otherwise exist.

By virtue of the amendment, the Illinois law is controlling. The General Banking Act of Illinois does not permit a pledge of assets to secure deposits. The Illinois statute authorizes the formation of banking associations "for the purpose of discount and deposit * * and doing a general banking business * *". No statute can become effective in Illinois affecting the charter power of banks unless submitted to and approved by popular vote. If the general provisions of the Banking Act authorize the pledging of assets to secure public deposits they equally authorize pledges to secure private deposits. *Ward* v. *Johnson*, 95 Ill. 215, does not involve any question as to general deposits of the kind dealt with in the instant case, nor does it involve the provisions of the General Banking Act. The bank there was operating

under a special charter with special provisions therein as to deposits. The essential question there decided was whether that bank could borrow money and issue "investment certificates" therefor. The most recent case in the Appellate Court of Illinois (certiorari denied by the Supreme Court) recognizes the principle of those cases holding pledges of assets to secure deposits to be invalid in the absence of express statutory authority. The common law right of priority in the sovereign is in Illinois limited to moneys belonging to the state. It does not apply to moneys of a political subdivision thereof. The right of priority in Illinois is not the equivalent of a specific lien.

The policy of a state or of the United States is that declared by the constitution and valid laws thereof, or in the absence thereof, by the courts. The legislature, however, can declare a policy with respect to specified classes of deposits and may provide that public deposits may or must be secured by specific pledges of assets. Failing such statutory declaration of policy, however, it is not within the province of the judiciary to declare a policy limited to public deposits alone. A general policy against permitting the securing of deposits, including both public and private deposits, yields only to such specific declaration of policy as there may be in the case of public deposits. Such a specific declaration of policy, if any, in the case of public deposits, must be found in those specific statutes authorizing or directing such pledges to be made.

The receiver may reclaim the securities pledged, leaving the depositor to his general claim against the receivership or to such other rights or remedies as the particular circumstances permit. The receiver does not stand solely in the shoes of the bank. He is the representa-

tive of the creditors and depositors. Pledges to secure deposits, if invalid, are invalid not merely as *ultra vires* of the bank, but are invalid as against the creditors and depositors generally. Such creditors and depositors, through their representative the receiver, are therefore claiming in their own right and not merely through the bank. The securities pledged are admittedly the property of the bank and should be returned to the receiver for the proper administration thereof, leaving to the proper form the determination of all priority or trust claims. If the City of Marion has any claim against the bank on any elements of fraud or trust, those claims may be asserted in the proper form. Even if such claims existed and should be ultimately sustained, still the present pledge should not be enforced. A right growing out of fraud or some trust relationship is but a priority claim and is not the equivalent of a specific lien.

I.

THERE IS NO GENERAL POWER UNDER THE NATIONAL BANKING ACT PERMITTING A NATIONAL BANK TO PLEDGE ITS ASSETS TO SECURE DEPOSITS.

The essential premise of appellants' case is that Section 8 of the national banking Act confers upon a national bank the power to pledge its assets to secure deposits, the seventh subdivision of which empowers a national bank to exercise "all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; * * *." No power to pledge assets to secure deposits is given in terms. Such power, if it exists, must therefore be found somewhere in the language above

quoted. In this regard we pass for the moment the effect of Section 45 of the Act.

In considering the effect of Section 8, it is apparent that the related question in No. 128 must be kept in mind for if the power to pledge assets to secure deposits is to be found in Section 8 then, we submit, there can be no distinction made between a pledge to secure the deposit of public funds and a pledge to secure a deposit of private funds. Any distinction to be made between those two kinds of deposits must be found elsewhere in the banking Act or in some other applicable statute.

Peculiarly enough appellants do not apparently question the holdings in *Smith* v. *Baltimore & Ohio Rd. Co.*, (C. C. A. 3) 56 Fed. (2d) 799, affirming 48 Fed. (2d) 861, and *Texas & Pacific Ry. Co.* v. *Pottorff*, (C. C. A. 5) 63 Fed (2d) 1, which latter case is No. 128 in this court, notwithstanding that their argument, based upon the cases cited at page 12 of their brief, would indicate that private and public deposits stand upon the same footing.

Section 45 of the banking Act requires the Secretary of the Treasury to require national banks to give satisfactory security by the deposit of United States Bonds and otherwise for the safe-keeping and prompt payment of public money deposited with them and for the faithful performance of their duties as financial agents of the government. We submit that in the case of national banks where the statute in form is a mandate to the public officer to require a national bank to give security, the statute is also a delegation of power to the bank to give the security required. Even there the statute has reference only to public moneys of the United States (*Coudert, Adm.* v. *United States,* 175 U. S. 178; *Branch* v. *United States,* 100 U. S. 673). Similar statutes dealing with deposits of a *quasi* federal or *quasi* public charac-

ter have, we submit, the same legal effect as amounting to grants of power to national banks to make the required pledge.

The court below in the majority opinion expressed doubt as to whether these statutes were to be regarded as grants of power because of the fact that many of them in terms refer to state books and obviously a federal statute cannot, generally speaking, affect the charter powers of state banks. In its opinion the court below said "Hence we conclude that in enacting those statutes Congress did not intend to create additional power for national banks in the respect mentioned, but incidentally recognized a power which it thought already existed under a former statute". We respectfully suggest, however, that the question is not essentially what Congress may or may not have thought about the matter but is as to the legal effect of a statute which requires the giving of such security. For example, supposing either as a matter of construction or by express wording a national bank is forbidden by the general banking Act to pledge its assets for any kind of deposit. Assume then a statute is subsequently passed in the same form as Section 45 of the Act—would it not follow that as a matter of statutory construction the statute would operate as a delegation of power and would suspend the general prohibition of the statute to the extent of the kind of deposit for which security must be given? We suppose that for most purposes, practically at least, there is no difference between an expressed grant or a grant by implication or a "recognition" of some power otherwise existing or otherwise thought to be existing. In either and all events the power to make the pledge is supplied by the statute.

A.

A NATIONAL BANK HAS NO GENERAL POWER TO PLEDGE ITS ASSETS TO SECURE PRIVATE DEPOSITS.

As we have said, the courts of appeal for the Third and Fifth Circuits agree that national banks may not pledge their assets to secure private deposits. One of the most recent cases in the state courts upon this subject is *State Bank of Commerce* v. *Stone,* 261 N. Y. 175; 184 N. E. 750. There the court pointed out the distinctions between a loan and a deposit and held that the power to pledge assets to secure a private deposit did not exist, and in referring to certain statutes dealing with public deposits the court said that an act of the legislature "was evidently thought necessary even as to public moneys to enable banks to pledge certain securities or undertakings or deposits". The court there adopted and applied to private deposits the same principle under which the courts of Minnesota, Kentucky and North Dakota had condemned pledges to secure public deposits not within the terms of the statutes authorizing such pledges.

While the question of policy involved in these cases was the subject-matter of discussion both in the majority and minority opinions in the court below, we stress the fact that the practice of pledging assets must of necessity be carried on in secrecy to prevent the withdrawal by other depositors of their deposits without like security which is itself sufficient indication of its vicious tendency. (Cf. *Farmers etc. Bank* v. *School Dist.* 174 Minn. 286; 219 N. W. 163)

The 1930 amendment does not deal with private deposits, nor does Section 45 deal with private deposits excepting insofar as the argument is made that Section 45

enjoins a duty upon the Secretary of the Treasury to require the giving of security for certain deposits and that said Section 45 merely "utilizes" in certain cases a power which is otherwise conferred upon the bank through other provisions of the Act.

A comparatively few only of the cases involve private deposits. *Ward* v. *Johnson,* 95 Ill. 215, affirming 2 Ill. App. 261 involved a special charter and did not involve at all a deposit in the sense dealt with in the present case. The General Banking Act of Illinois was in no way involved.

Ahl v. *Rhoads,* 84 Pa. 319, is sometimes cited as an authority supporting the right of a bank generally to pledge its assets to secure deposits, including private deposits. In that case the bank, which had been organized under a special act, transferred to the plaintiff (who was a director of and a depositor in the bank) as collateral security for the deposit a certain mortgage held by the bank. The mortgage was foreclosed by the bank with the plaintiff's consent on condition that the bank would thereafter execute to him a mortgage on the same land after the bank had acquired title. Thereafter the bank executed the mortgage to the plaintiff and the plaintiff agreed that the amount which he had formerly had on deposit should not be subject to check but should be repaid to him one year thereafter. Subsequently the bank failed. The principal question was as to the power of the bank to execute the mortgage without the consent of the holders of a majority of the stock. The opinion treats the transaction as one in which collateral is given to secure an indebtedness in the nature of a loan.

In *Cameron* v. *Christy,* 286 Pa. 405, 133 Atl. 551, the statute authorized trust companies "to receive deposits of money and other personal property and issue their

obligations therefor." The case involved public deposits but the court construed the statute as authorizing the giving of security. Among other things, as appears from the opinion, the parties agreed that the pledging of assets by banks to secure public deposits was a matter of general practice in Pennsylvania.

In *Schumacher* v. *Eastern Bank & Trust Company* (C. C. A. 4) 52 Fed. (2nd) 925, a national bank had procured certain loans from a state bank to secure which certain notes and other securities of the national bank were pledged as security. The amounts so advanced by the state bank were carried on the books as "due from banks" and "due to banks". No deposit account was opened for the state bank, no certificates of deposit were issued and the amounts advanced were not reported by the national bank as deposits. The state bank never at any time attempted to check against the advances, the whole matter, as the court said, being handled by both banks as an indebtedness. The pledges were sustained, and of course properly so if the transactions were loans, as there is no question made but that a bank may borrow money and give security therefor. The court should also bear in mind the somewhat peculiar relationship between banks themselves in making advances to each other, whether in one form or another. Generally, such advances, although in the form of "deposits", are in effect nothing but loans (Cf. *Bank* v. *Lanier,* 11 Wall. 369).

In *Button* v. *Sanguinetti* (Ariz. 1932) 11 Pac. (2nd) 1085, the earlier case of *Williams* v. *Hall,* 30 Ariz. 581, 249 Pac. 755, was limited to a case of loan. It was held that a bank has no general power to pledge assets to secure general deposits and that the power to pledge certain assets to secure public deposits rested upon statute. Referring to those statutes the court said: "This language

does not expressly nor impliedly authorize a bank to give security to depositors of private moneys, and the best-reasoned cases hold that such power is not incidental nor essential to good banking practices".

It is competent, of course, for any state acting within the confines of its own constitution to authorize its own banks to pledge assets to secure deposits of any type or character or to place any limitations or restrictions thereon as it sees fit. In other words, any state has unquestioned power to declare its own policy with respect to banking business conducted within its borders by its own banks. The question is not as to the power of the state to act in that regard but it is a question as to whether the bank has been given the power. In the instant case the record is silent as to any established practice in Illinois of making such pledges and although the briefs suggest that in very recent times public officers without specific statutory authority have exacted security, no claim is made that any such practice has been adopted or has prevailed in the case of private deposits. We are confident that the court will appreciate that the pledging of assets to secure a private deposit is not incidental or reasonably necessary to carry on the business of banking within the legal meaning of the doctrine as to implied powers.

We submit, therefore, that viewed from the standpoint of a private deposit, we must start with the premise that the general power to conduct a banking business and to receive deposits does not by implication carry with it power to pledge assets to secure such deposits.

B.

A NATIONAL BANK HAS NO GENERAL POWER TO PLEDGE ITS ASSETS TO SECURE PUBLIC DEPOSITS.

The same general principles, we submit, apply as to pledging assets to secure public deposits as apply to a pledge to secure private deposits. We cannot understand how Section 8 of the General Banking Act grants power to pledge assets to secure public deposits and at the same time withholds power to make a pledge to secure private deposits. It may of course be desirable that public deposits be placed in a separate category and be secured by specific pledge. The public at large is obviously greatly concerned in the safety of public funds, whether state or national. While in the states generally there is recognized a common law right of priority in payment, except as modified by statute, there is no such right of priority in the case of the United States or any of its public offices. As the opinion of the court below points out and as the unquestioned rule is in the case of the United States and its public offices, priority in payment depends wholly upon statute. It has been suggested that the power to pledge is the equivalent of the common law right of priority. The analogy, however, does not hold. In Illinois, for instance, the right of priority extends only to moneys belonging to the state itself. It does not apply to moneys of any of the political agencies of the state. (*People* v. *Marion Trust & Sav. Bk.*, 347 Ill. 445; *People* v. *West Englewood Trust & Sav. Bk.*, 353 Ill. 451; 187 N. E. 526. However, such right is a right of priority only and not of specific lien. The priority exists only as against general creditors or deposits of the bank, and the priority may be subject to a process of prorating with other priority creditors. A lien claimant on the other hand has a right to

have the fund pledged exhausted for the payment of his claim. As to the assets pledged, the right of the depositor is paramount both to general creditors and depositors and to priority creditors not holding a specific lien. For an analysis and classification of the numerous cases upon the subject of pledging assets to secure public deposits, we refer to the majority opinion below. We shall attempt no review of them in this brief. We ask the court, however, to bear in mind in considering those cases which sustain a pledge to secure public funds merely because there is no express prohibition in the statute against such pledge that such holdings have the effect either of wiping out any distinction between public and private deposits or else are an attempt on the part of the courts to declare a policy as to a specific type of deposit, a matter which is solely within the province of the legislative branch of the government.

The two cases which can perhaps be regarded as forming the basis for those holdings sustaining a pledge to secure public deposits are *Richards* v. *Osceola Bank*, 79 Ia. 707, 45 N. W. 294, and *McFerson* v. *National Surety Co.*, 72 Colo. 482, 212 Pac. 489. Both cases dealt with the question summarily and without the citation of authority. The reasoning in the Colorado case would apply equally to private deposits. The reasoning in the Iowa case would also seem equally applicable to private deposits, or if not, then the court has declared a policy for a single class of deposits, a power which we have said does not belong to the judicial branch of the government. In a later Iowa case, *Andrew* v. *Odebolt Sav. Bank*, 203 Ia. 1335, 214 N. W. 559, the earlier holding was approved and the court inquired as to whether there was any logical reason "why the bank may not legally transfer any portion of its assets in good faith to the county or any other depositor in payment of or as secur-

ity for deposits of public funds?" It was said that the bank might have sold the assets and paid the deposits. The court's reasoning is not convincing and its conclusion is not a necessary consequence of its premise. If the bank sells its assets the depletion in assets is offset by a corresponding decrease in deposit liabilities. If money is borrowed to pay depositors, the liabilities remain the same, which, however, could be said if sufficient were borrowed to pay all of its depositors. In that event the bank would cease to function as a bank of deposit (Cf. *Farmers State Bank of Gatzke* v. *County of Marshall,* 175 Minn. 363, 221 N. W. 243).

We admit that there is or may be a strong urge on the part of any court to protect what seems to be the public interest by sustaining a pledge made without statutory support other than may be found in the general authority to conduct the business of banking and to receive deposits. The history of the last few years may have crystallized this natural tendency. There is, however, implied in a general way, in the business of banking, the question of equality between depositors, subject only to those well-defined exceptions where rights of priority exist either in the case of public deposits or sometimes in the case of private deposits where elements of fraud or of trust intervene. And as has been pointed out, the question does not arise in all its magnitude until the bank has closed its doors. It may be said that any taxpayer has the right to exact security and to refuse to deposit his money in the bank unless such security is given, but if all depositors took that position and acted upon it, it seems to us very apparent that the bank would either have no free assets or it would have no deposits. In neither event could the bank function as a bank.

III.

THE 1930 AMENDMENT GAVE TO A NATIONAL BANK ONLY THE SAME POWER TO PLEDGE ITS ASSETS TO SECURE PUBLIC DEPOSITS OF THE STATE OR SOME POLITICAL SUBDIVISION THEREOF AS A STATE BANK WITHIN THE SAME LOCALITY POSSESSES.

It is not unusual for the Congress, to the extent it may lawfully do so, to create parity between state and national banks within the same locality. Branch banking is but one illustration. National banks acting as trustees within the given state is another illustration. Congress may, therefore, either grant to national banks the same power possessed by state banks within the same locality, or if the power of national banks were otherwise greater than the local banks, Congress could restrict the power of national banks to those exercisable by the local banks. It is argued by appellants and in the minority opinion below that the 1930 amendment was an extension of the powers of national banks rather than any abridgment thereof. To the extent that it conferred upon national banks the power to pledge assets to secure the deposits of the state or some political subdivision thereof, and which power did not theretofore exist, we agree that the 1930 amendment was an enlargement of the powers of national banks and was a delegation of authority to them to make such pledge. If, however, we start with appellants' premise that the power to make such a pledge as is specified in the amendment existed prior to the amendment and wholly apart thereof, then the amendment must operate as a restriction upon the powers of national banks or else the amendatory act was wholly surplusage. We cannot understand how upon appellants' premise the amendment can be regarded as an enlargement of the powers of national banks. The

power asserted by appellants as existing under the general provisions of the Banking Act and by implication therefrom is without limitation of any kind. If any specific asset can be pledged by the bank then all of its assets can be so pledged. The minority opinion suggests that it was intended to do away with any prior inhibitions upon national banks. There is no suggestion made as to what those inhibitions were or might be. A general power to pledge assets without more has no inhibitions and no other enactment is pointed out which would operate as an inhibition upon the power. It is not to be presumed that Congress intended to do an unnecessary thing and nothing in the record submitted with respect to the enactment of that amendment is sufficient to indicate such to be the case. Certainly if nothing more was intended than to merely confirm an existing power, we can see no occasion for that part of the amendment which establishes equality between the national and the state bank within the same locality. If the state bank had the power to pledge its assets to secure the deposits of the state or any of its political subdivisions then Congress intended that a national bank should have the same power and none other. This equality exists under the amendment only with respect to the deposits of the state or its political subdivisions. Under the reasoning of the minority opinion below a national bank can pledge its assets to secure private deposits or any other type of deposit other than those of the state or some political subdivision thereof, wholly without regard to whether a state bank within the same locality could make such pledge. There would be no equality or parity between a national and a state bank within the same locality as to such deposits. We have seen no convincing suggestion as to why the Congress

should establish such equality between a national and a state bank merely as to state deposits.

It has been said upon one or more occasions that the Comptroller of the Currency has consistently ruled apart from the 1930 amendment that a national bank may properly pledge its assets to secure public deposits. We are not advised as to whether such rulings refer only to the deposits of the kind mentioned in the various special statutes, whether they apply to deposits made by a state or some political subdivision thereof without regard to whether a state bank within the same locality may make such pledge, or whether they include deposits of a kind having some resemblance to public deposits such as receivers. Even there, there is no claim that it has been the ruling of the Comptroller that private deposits may be so secured. We respectfully submit, therefore, that the fact, if it be a fact, that such rulings had been made with respect to public deposits generally, adds nothing of force to the question to be determined, but that the question in its entirety should be independently determined.

It is said by petitioners in their Summary of Argument (Br. p. 9) that with the exception of Judge Sparks' opinion in the present case, all other expressions of the Federal Courts as to the effect of this amendment support the petitioners' contention that the amendment did not withdraw from national banks power previously existing. We challenge the accuracy of that statement.

In *Feather* v. *School District,* United States District Court, Western District of Pennsylvania (Petitioners' Br. p. 20), the court based its decision upon the amendment and the further fact that it conceived that the Pennsylvania Supreme Court had sustained such pledges.

In *Pottorff* v. *El Paso-Hudspeth Counties Rd. Dist.*

(C. C. A. 5) 62 Fed. (2d) 498, the decision was rested upon the fact that the Texas statute authorized the pledge. In no other way could the Texas rule have been made controlling other than through the 1930 amendment. The amendment in so far as it deals with powers of national banks is surplusage upon appellants' theory of the case.

IV.

THE GENERAL BANKING ACT OF ILLINOIS DOES NOT PERMIT SUCH PLEDGE.

In considering this question the court must keep in mind—first, the provisions of Section 5 of Article XI of the Illinois Constitution which provides that no statute "authorizing or creating corporations or association with banking powers, whether of issue, deposit or discount, nor amendments thereto, shall go into effect or in any manner be in force unless the same shall be submitted to a vote of the people at the general election next succeeding the passage of the same, and be approved by a majority of all the votes cast at such election for, or against such law" and second, the rule of the Illinois Supreme Court upon the subject of implied powers of corporations.

The right of a bank, if any, to pledge its assets to secure deposits depends upon the extent of its charter powers. The argument of appellants is in effect that the right to pledge assets to secure deposits is incidental to, or implied from, the power to conduct the business of banking and to receive deposits. Any statute, therefore, which confers upon Illinois banks the right to pledge its assets to secure deposits is within the constitutional provision and is ineffective unless submitted to and ap-

proved by popular vote. The referendum provision of the statute refers "to the manner of organization of banking corporations, the privileges granted to them, the duties and obligations imposed upon them, the supervision, regulation and control of them by the Auditor, and not to the general rules of commercial law, the law of negotiable instruments, and the great mass of substantive law to which the Banking act makes no reference" (*People* v. *Gould*, 345 Ill. 288, 302-3). Even though a statute is of general application and applies to other corporations, if it in effect deals with the charter powers of a bank or any of its essential functions, it is invalid and inapplicable to banks without a referendum (*Golden* v. *Cervenka*, 278 Ill. 409; *Reed* v. *People*, 125 Ill. 582; *Sykes* v. *People*, 132 Ill. 32.)

The relevancy of the referendum provision of the Illinois constitution is apparent when considered in the light of appellants' argument that a statute may "recognize" a power in a bank to pledge its assets to secure deposits. Such "recognition" is wholly ineffective in Illinois unless the power claimed to be "recognized" is itself found in some statute which has met the test of the referendum. In the case of national banks and so far as concerns the National Banking Act and other federal statutory enactments, the theory of recognition is, we submit, a misnomer. The power claimed must be found either in some statute other than that in which the "recognition" is made or else the statute which recognizes the power is in legal effect a grant of such power.

In connection with the referendum provision appellants question the holding of the court below with respect to the Commission Form of Government Act which provides for the giving of bond by the bank to secure the deposits there mentioned. It is said that that statute can-

not abrogate the power of the bank to make a pledge which otherwise exists under the General Banking Act because not submitted to referendum, and that therefore the Commission Form of Government Act is ineffective to strike down such pledge. We point out, however, in this regard that under proper circumstances a statute can prohibit in particular cases the exercise of an otherwise existing power without abrogating the power itself. A statute we conceive may properly be held to be valid which in terms provides that a bank shall not pledge its assets to secure some particular type of deposit. On the contrary, if the power to pledge assets in general is not found in the General Banking Act then any statute which delegates that power to a bank must be submitted to referendum.

A.

AN ILLINOIS BANK HAS NO IMPLIED POWER TO PLEDGE ITS ASSETS TO SECURE DEPOSITS.

The books are full of cases discussing the nature and extent of the implied powers of a corporation. In Illinois the rule is that corporations can exercise only such powers as are conferred by the legislative body creating them "either in express terms or by necessary implication" and that implied powers are presumed to exist to enable such bodies to carry out the express powers granted and to accomplish the purposes of their creation. (*People* v. *Chicago Gas Trust Co.*, 140 Ill. 268.

In *Calumet, etc. Dock Co.* v. *Conkling*, 273 Ill. 318, the loan of money by a corporation was held void although made as part of a transaction whereby the corporation was endeavoring to sell a portion of its real estate. In that case it was said that an "implied or incidental power

must be directly or immediately appropriate to the execution of the powers expressly granted and not one that has a slight or remote relation to it" and that a "power which the law will imply must be one in a sense necessary or needful and suitable to accomplish the object for which the express powers were granted". Among other cases the court cited *Central Transportation Co.* v. *Pullman Palace Car Co.*, 139 U. S. 24.

In Illinois, therefore, a power will not be implied merely because its exercise may be of some benefit or advantage to the corporation. The essential consideration is that the implied power must be one which will enable the corporation to exercise the powers expressly conferred upon it, as it is not to be presumed that the state would authorize the corporation to carry out its objects and at the same time deny to the corporation the necessary to reasonable means of so doing. Nowhere in any discussion that we have seen of the general question now under consideration has it been claimed or thought that the power to pledge its assets to secure any of its deposits, either public or private, was in any way essential to the carrying on of the bank's business of receiving deposits. On the contrary, as the Supreme Court of Minnesota has said (*Farmers etc. Bank* v. *School Dist.*, 174 Minn. 286, 219 N. W. 163), the indulgence in any such practice is conducive to the destruction of the bank. Furthermore, nothing in the record now before this court indicates the necessity of any such power to enable banks to function as banks of deposit.

That a sovereignty may by valid statute declare a public policy of authorizing and empowering banks to pledge assets to secure the funds of the sovereignty, as Congress has done in the case of the National Bank Act, is no indication that the power exists either as to public or

private funds in the absence of such express statutory authority. On the contrary, the existence of such a statutory declaration of policy is strong evidence that without it the power claimed does not exist.

So far as the law of Illinois is concerned, the question is as to whether the General Banking Act confers power upon banks organized thereunder to pledge its assets to secure the payment of deposits either public or private—in the instant case to secure public deposits of a municipality. In this regard we lay to one side for the present the question as to the Commission Form of Government Act. It is argued by appellants—first, that *Ward* v. *Johnson,* 95 Ill. 215, is a decision holding that such pledges may be made, and secondly, that whether or not it does so hold certain of the language in the opinion in effect states that such pledges may be made and that the General Banking Act was enacted in the light of this language, with the result that the General Banking Act is to be construed as conferring such power. It is obvious from a mere cursory reading of the case that it did not involve deposits of the kind involved in the instant case; nor was the General Banking Act there involved. The exact question decided in that case was as stated by the court in the opinion whether the bank had "power to borrow money and issue 'investment certificates' therefor, secured by trust deed as was here done." The bank was organized under a special act of the legislature and the statute empowered the bank "to make such special regulations with reference to trust funds, deposits or savings as shall best aid the depositors and parties interested". There the certificates in question were in fact investment certificates. There was no general obligation on the part of the bank to repay the certificates but there were redeemable either by exchanging them for

specific securities held by the trustee or were redeemable in cash not out of the general funds of the bank but solely out of the proceeds derived from the collection or sales of the securities so pledged. The transaction there dealt with in the event the investment certificates were exchanged for the securities pledged with the trustee, constituted rather a sale of such securities and if they were redeemed in cash out of the proceeds derived from such securities, the transaction constituted in effect a loan. The District Court in this case recognized that the question decided in *Ward* v. *Johnson* differed from that in the case at bar but stated that the broader principle therein expressed had never been questioned in Illinois by any decision or by any legislative enactment. The case, however, so far as the question involved was concerned involved no broad principle and no occasion has arisen to consider that decision from the standpoint of general deposits of the kind involved in the instant case. In one Appellate Court case (*Lamb* v. *Fidelity & Deposit Co.* 257 Ill. App. 262, certiorari denied by the Supreme Court) nothing was involved in the way of a pledge but the case dealt with the rights of a surety company which had become surety upon the County Treasurer's general bond as against certain personal sureties who had agreed to indeminify the surety company against liability. The right or power of a bank to execute a depositary bond to secure a deposit is wholly different from the right or power to pledge assets as security therefor. (Cf. *Farmers etc. Bank* v. *School Dist.* 174 Minn. 286, 219 N. W. 163; *Leonard Co-op. Creamery Assn.* v. *First State Bank*, 168 Minn. 28, 209 N. W. 631.)

In *People* v. *Seward State Bank*, 268 Ill. App. 32, the court in the course of its opinion approved *Commercial Bank & Tr. Co.* v. *Citizens Trust & Guaranty Co.* 153 Ky.

566, 156 S. W. 160, saying with reference to the General Banking Act that it "contemplates fair and uniform dealing by banks with all their depositors and any secret agreement to protect one while others are left without security, even though no actual fraudulent intent is apparent, is nevertheless absolutely void and of no effect." The case involved an alleged trust or special deposit. Certiorari was denied.

As we have stated before, most of the cases are classified and reviewed in the majority opinion below. The recent tendency is in the direction that such pledges are invalid in the absence of some specific statutory authority (*State Bank of Commerce* v. *Stone,* 261 N. Y. 175, 184 N. E. 750; *Foster* v. *City of Longview* (Tex. Com. App.) 26 S. W. (2d) 1059; *Austin* v. *Lamar County* (Tex. Com. App.) 26 S. W. (2d) 1062).

In the two cases from the Fifth Circuit (*Pottorff* v. *El Paso-Hudspeth Counties Rd. Dist.* (C. C. A. 5) 62 Fed. (2d) 498 and *Texas & Pac. Ry. Co.* v. *Pottorff* (C. C. A. 5) 63 Fed. (2d) 1, the latter case being No. 128 in this court, the court denied any general power in a national bank to pledge its assets to secure deposits but sustained the power to pledge assets to secure deposits of local municipalities on the ground that the Texas statute authorized such pledges and that the Texas statute was made controlling by virtue of the 1930 amendment.

In the cases from the District Court for the Western District of Pennsylvania (Appellant's Br. pp. 20-21) a general power to pledge was denied but as we view it the 1930 amendment was recognized as controlling as to deposits of a local municipality and the local rule in Pennsylvania was applied. The case from the District Court for the District of Connecticut (Appellants' Br. p. 21) in making a distinction between public and private deposits

without the support of statute is but another example of judicial legislation. No court has the right to declare a policy in such fashion. The case from the Tenth Circuit (Appellants' Br. p. 25) also recognizes the controlling effect of the 1930 amendment where it applies in effect the Colorado rule.

Appellants refer to Section 11 of the Illinois Banking Act as amended in 1929 directing that receivers of closed banks shall take security for such deposits. That amendment was submitted to referendum and therefore may validity add to the charter powers of banks. The same principle applies to that provision as applies to Section 45 of the National Banking Act. A direction to the receiver to require such pledge carries with it by necessary implication the necessary implication the necessary power to the bank to make the pledge. This is not, as appellants claim, an expression of the general policy that Illinois banks should have the power to pledge their assets to secure any and all deposits but was an express declaration of policy that banks could and must secure deposits made by receivers of closed banks.

Reference is made to the State Depositary Act, which in terms requires the giving of security for deposits of state money. The Attorney General, however, has ruled that the statute is invalid because not submitted to referendum, also that none of the Illinois statutes authorizes or empowers an Illinois bank to pledge its assets to secure deposits of any kind (Op. Atty. Gen. 1930, p. 457; Op. Atty. Gen. 1931, p. 1).

Appellants cite in their brief some of the decisions in the various states as supporting their contentions. As we have said before, we shall not undertake a review of these cases. Careful reading of them will disclose the grounds on which they are based. Appellants refer to

the cases holding such pledges to be invalid in the absence of requisite statutory authority as expressing the "minority view". A reading of the cases, however, will indicate that most of the cases relied upon by appellants to support their views are in reality based upon some measure of statutory authority. Few if any of them go to the extent of holding that a mere general authority to conduct a banking business or to receive deposits carries with it the authority to pledge assets to secure such pledges. A negligible few involve private deposits at all. As we have said upon the general premise that the general power to conduct a banking business and to receive deposits implies authority to pledge assets to secure such deposits, no distinction can be made between public and private deposits. Therefore, wherever in those jurisdictions a distinction between those two types of deposits is made, a holding in support of a pledge for a public deposit is necessarily either based upon statutory authority or else the court is itself in declaring a policy in that regard, in evading in that regard the province of the legislature.

Appellants refer in their brief, at p. 57, to various state statutes requiring the giving of security. The argument is that these statutes refute any idea that the making of such pledges is contrary to public policy. Appellants, however, seem to overlook the fact that the policy is what the legislature declares it, and no one heretofore has questioned the right of any state by valid enactment to declare a policy with respect to public deposits which does not or might not apply to private deposits. That is the point that we have been endeavoring to make that if such pledges are to be made they must be made under direct statutory authority.

V.

THE RECEIVER IS ENTITLED TO RECLAIM THE SECURITIES.

There is some divergence of view as to whether if a pledge is invalid the securities may be reclaimed by the receiver. In Illinois at least a receiver of a closed bank is a direct representative of the creditors and is not merely standing in the shoes of the bank (*Golden* v. *Cervenka,* 278 Ill. 409). In one aspect of the question, the pledge, if invalid, is invalid not merely as to the bank because in excess of its charter powers, but is invalid as against other creditors and depositors. In that sense the creditors or depositors through their direct representative the receiver have a standing to insist that the securities pledged be returned. They are not necessarily claiming through the bank. The question does not always arise in the same manner as it has arisen in the instant case—for example, in the case in which the writer of this brief is involved, the action was brought by the surety company to compel the application of the securities to the payment of the deposit; in other words, the surety company is in court asking the enforcement of the lien. The receiver is defending against that position. In the instant case the securities are in the possession of a third party and the receiver is attempting to compel their return to him for proper administration. The defendants there are asserting their claim to such securities, the surety company being really in the guise of the principal claimant. It was the surety upon the official bond of the City Treasurer and it is in the position of affirmatively asking for a right of subrogation and the enforcement in the name of the Village Treasurer of the pledge attempted to be made. Appellants finally suggest that if the deposits were made in violation of the

statute, they should be regarded as in the nature of a trust fund. We submit that the record does not permit such an adjudication. No such relief was prayed in the pleadings and all that is required to be done under the judgment of the court below is that the assets in question, admittedly the property of the bank, be returned to the receiver for proper administration. If appellants have any claims against the receiver on the theory that the fund is a trust fund, it may now make proper application therefor. Even there the right is one of priority rather than of specific lien. It is for the receivership court to determine any such question raised by appellants and to determine priorities in orderly fashion.

Two other briefs have been filed as *amici curiae*—one on behalf of the Philippine Islands, and one on behalf of the City of Chicago. Both briefs stress the question of expediency which is involved. We beg to point out that the banking tragedies which have occurred within the past few years have demonstrated an urgent need for a thorough revision of our banking laws generally, both as to substantive matters and as to questions of administration. Expediency, however, is not a substitute for sound principle.

So far as the City of Chicago is concerned, the suggestion seems to be that certain city ordinances authorizing or requiring a pledge of assets is sufficient authority to the bank to make the pledge. Obviously the powers of an Illinois bank depend upon the statute under which it is created, not upon ordinances of the City of Chicago.

We respectfully submit that the judgment of the court below should be affirmed.

Respectfully submitted,

LELAND K. NEEVES.

APPENDIX.

Law Offices of

FERRELL AND HAY

First National Bank Building

Marion, Illinois

November 3, 1933

Mr. Leland K. Neeves
Scott, MacLeish & Falk
134 S. La Salle Street
Chicago, Illinois

Re: City of Marion, Illinois, a municipal corporation, Continental Illinois Bank & Trust Company, a corporation, The Fidelity & Casualty Company of New York, *et al.*, Petitioners, *v.* Ben Sneeden as Receiver of City National Bank of Herrin, Illinois, Respondent. No. 400, Supreme Court of the United States, October Term, A. D. 1933.

DEAR SIR:

We hereby consent to your filing a brief in the above entitled cause as *amicus curiae.*

HOSEA V. FERRELL,
JOHN HAY,
Attorneys for Respondent.

MAYER, MEYER, AUSTRIAN & PLATT
Continental Illinois Bank Building
Chicago

October 21, 1933.

Mr. Leland K. Neeves
Of Scott, MacLeish & Falk
134 South LaSalle Street
Chicago, Illinois

DEAR SIR:

Re: City of Marion *v.* Sneeden (No. 400, October Term, 1933, Supreme Court of the United States

Referring to the request contained in your letter of the 20th inst., we, as counsel for Continental Illinois National Bank and Trust Company, have no objection to your filing a brief as *amicus curiae* in the above entitled cause. As you know we represent no party other than the Bank.

Yours very truly,

MAYER, MEYER, AUSTRIAN & PLATT.

DFR

Law Offices

POPE AND DRIEMEYER
24 North Main Street
East St. Louis, Illinois

October 27, 1933.

Mr. Leland K. Neeves,
Scott, Mac Leish & Falk,
Attorneys at Law,
134 South LaSalle Street,
Chicago, Illinois.

DEAR SIR:

Re: Sneeden *v.* City of Marion.

This will acknowledge your letter of October 26th.

We do appear in this case for all of the defendants except Continental Bank, and we will not interpose any objections if you ask leave of the Supreme Court to file a brief as *amicus curiae.*

Very truly yours,

POPE & DRIEMEYER
By HENRY DRIEMEYER

HFD:RM.

CC to Messrs. Mayer, Meyer, Austrian & Platt.